

SUMMARY ANALYSIS OF AMENDED BILL

Franchise Tax Board

Author: Leach Analyst: Paul Brainin Bill Number: AB 8

Related Bills: _____ Telephone: 845-3380 Amended Date: 05-11-98

Attorney: Doug Bramhall

Sponsor: _____

SUBJECT: Minimum Tax/Dissolved or Withdrawn Corporations, Limited Partnerships, Limited Liability Companies, and Limited Liability Partnerships

DEPARTMENT AMENDMENTS ACCEPTED. Amendments reflect suggestions of previous analysis of bill as introduced/amended _____.

☒ AMENDMENTS IMPACT REVENUE. A new revenue estimate is provided.

AMENDMENTS DID NOT RESOLVE THE DEPARTMENT'S CONCERNS stated in the previous analysis of bill as introduced/amended _____.

FURTHER AMENDMENTS NECESSARY.

DEPARTMENT POSITION CHANGED TO _____.

☒ REMAINDER OF PREVIOUS ANALYSIS OF BILL AS INTRODUCED/AMENDED April 28, 1998 STILL APPLIES.

☒ OTHER - See comments below.

SUMMARY OF BILL

This bill would amend sections of the Personal Income Tax Law (PITL) and Bank and Corporation Tax Law (B&CTL) of the Revenue and Taxation Code (R&TC) to prorate the final annually imposed tax due for the year of dissolution or withdrawal of corporations, limited partnerships (LPs), limited liability companies (LLCs), and limited liability partnerships (LLPs). The final tax amount shall be determined by multiplying the annual tax by the fraction, the numerator of which shall be the months of the taxable or income year, up to and including the month of effective date of dissolution or withdrawal, and the denominator of which shall be twelve.

SUMMARY OF AMENDMENT

The May 11, 1998, amendment added corporations and LPs to those entities which would be allowed to prorate their annual tax for the year of dissolution. This amendment also made changes to the PITL, instead of the B&CTL, to allow LLCs and LLPs to prorate their annual tax for the year of dissolution.

The amendment resolves the technical concern in the department's analysis of the bill as amended April 28, 1998, but raises another. This concern, as well as the prior policy and implementation concerns that apply and a new revenue estimate, are stated below. The remainder of the department's previous analysis still applies.

Policy Considerations

This bill would not provide equal treatment to other entities that pay an annual tax of a fixed amount such as real estate mortgage investment conduits (REMICs), financial assets securitization investment trusts (FASITs), and qualified subchapter S subsidiaries (QSSSs).

Board Position:

<input type="checkbox"/> S	<input type="checkbox"/> NA	<input type="checkbox"/> NP
<input type="checkbox"/> SA	<input type="checkbox"/> O	<input type="checkbox"/> NAR
<input type="checkbox"/> N	<input type="checkbox"/> OUA	<input checked="" type="checkbox"/> PENDING

Department/Legislative Director

Date

Gerald H. Goldberg

7/3/98

This bill would not provide equal treatment to entities with short period returns for reasons other than dissolution or withdrawal (e.g., mergers or reorganizations). According to the author's staff, it is not the author's intent to include entities filing short period returns for reasons other than ceasing to do business in this state.

Implementation Considerations

Refunds would need to be made to business entities that pay the applicable tax prior to the end of the taxable or income year, but subsequently are dissolved or withdraw before the end of that taxable or income year. Issuing these refunds would create a minor additional workload for the department.

Technical Considerations

This bill amends a section of the B&CTL providing for the calculation of the tax for the taxable year of dissolution. Since all other affected B&CTL provisions reference the minimum tax in Section 23153, this provision has been modified and moved to Section 23153 so that all other appropriate provisions will include the proration of the final year tax without the need to amend each of these sections.

This bill provides that for LLCs, LPs, and LLPs that dissolve or withdraw, the tax for the final year is prorated as specified. The date of dissolution for these entities generally precedes the date of the filing of the certificate that terminates the entities existence. The attached amendments clarify the termination date of these entities. These amendments also clarify that if the withdrawing entity continues to do business, the tax for the final year is not prorated.

FISCAL IMPACT

Tax Revenue Estimate

Based on data and assumptions discussed below, this bill would result in the revenue losses shown in the table.

Estimated Revenue Impact of AB 8 As Amended 5/11/98 [\$ In Millions]		
1998-99	1999-00	2000-01
(\$11)	(\$8)	(\$8)

The bill would be effective with income years beginning on or after January 1, 1998, with enactment assumed after June 30.

This analysis does not consider the possible changes in employment, personal income, or gross state product that could result from this measure.

Tax Revenue Discussion

The number of corporate and non-corporate entities that dissolve or withdraw in any given year and would owe a lesser amount of minimum tax than the currently required prepaid \$800 would determine the revenue impact of this bill.

The number of specified entities filing each year was projected by using an applicable growth rate for each entity type. According to departmental data, corporations terminate at a rate of approximately 3.5% annually (roughly 16,000 entities). The rate of corporate terminations was used as a proxy to determine potential terminations of other entity types eligible for this tax benefit. By assuming an average mid-year termination date, the above estimates were derived.

Before a corporation can be dissolved, surrendered, or merged by the Office of the Secretary of State, the Franchise Tax Board must issue a tax clearance certificate. A taxpayer must have prepaid the minimum franchise tax for its final year (account is current) to obtain a tax clearance certificate. Each year the department issues roughly 16,000 tax clearance certificates.

The revenue estimate for the prior version of this bill, which applied only to LLCs and LLPs, was a loss of \$1 million.

RECOMMENDATION

No recommendation.

At its May 28, 1998, meeting, the Franchise Tax Board considered this bill, but took no position. Controller Kathleen Connell was neutral, Member Dean Andal was in support, and the representative from the Department of Finance, was absent.

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FRANCHISE TAX BOARD'S
PROPOSED AMENDMENTS TO AB 8
As Amended May 11, 1998

AMENDMENT 1

On page 2, line 14, after "1997," insert:

(other than the taxable year of cancellation)

AMENDMENT 2

On page 3, delete lines 11 through 19, inclusive and insert:

(e) A limited partnership subject to tax pursuant to subdivision (b) for which a certificate of cancellation has been filed pursuant to Section 15623 or 15696 of the Corporations Code shall pay, for the taxable year of cancellation, a tax equal to the amount specified in paragraph (4) of subdivision (d) of Section 23153 applicable for the taxable year of dissolution or withdrawal of a corporation. This subdivision shall not apply to a limited partnership doing business in this state after the effective date of cancellation as provided in Section 15696 of the Corporations Code.

AMENDMENT 3

On page 3, line 20, after "SEC 2." insert:

Section 17941 of the Revenue and Taxation Code is amended to read:

17941. (a) For each taxable year beginning on or after January 1, 1997, every limited liability company doing business in this state (as defined in Section 23101) shall pay annually to this state a tax for the privilege of doing business in this state in an amount equal to the applicable amount specified in paragraph (1) of subdivision (d) of Section 23153 for the taxable year.

(b) In addition to any limited liability company which is doing business in this state and is therefore subject to the tax imposed by subdivision (a), for each taxable year beginning on or after January 1, 1997 (other than the taxable year of cancellation), a limited liability company shall pay annually the tax prescribed in subdivision (a) if articles of organization have been accepted, or a certificate of registration has been issued, by the office of the Secretary of State. The tax shall be paid for each taxable year, or part thereof, until a certificate of cancellation of registration or of articles of organization is

filed on behalf of the limited liability company with the office of the Secretary of State.

(c) The tax assessed under this section shall be due and payable on or before the 15th day of the fourth month of the taxable year.

(d) For purposes of this section, "limited liability company" means any organization that is formed by one or more persons under the law of this state, any other country, or any other state, as a "limited liability company" and that is not taxable as a corporation for California tax purposes.

SEC. 3.

AMENDMENT 4

On page 3, delete lines 22 through 36, inclusive, and insert:

17946. (a) A limited liability company shall not be subject to the taxes and fees imposed by this chapter if the limited liability company did no business in this state during the taxable year and the taxable year was 15 days or less.

(b) A limited liability company subject to tax pursuant to subdivision (b) of Section 17941 for which a certificate of cancellation has been filed pursuant to Section 17356 or 17455 of the Corporations Code shall pay, for the taxable year of cancellation, a tax equal to the amount specified in paragraph (4) of subdivision (d) of Section 23153 applicable for the taxable year of dissolution or withdrawal of a corporation. This subdivision shall not apply to a limited liability company doing business in this state after the effective date of cancellation as provided in Section 17455 of the Corporations Code.

AMENDMENT 5

On page 3, after line 36, insert:

SEC. 4. Section 17948 of the Revenue and Taxation Code is amended to read:

17948. (a) For each taxable year beginning on or after January 1, 1997, every limited liability partnership doing business in this state (as defined in Section 23101) and required to file a return under Section 18633 shall pay annually to the Franchise Tax Board a tax for the privilege of doing business in this state in an amount equal to the applicable amount specified in paragraph (1) of subdivision (d) of Section 23153 for the taxable year.

(b) In addition to any limited liability partnership that is doing business in this state and therefore is subject to the tax imposed by subdivision (a), for each taxable year beginning on or after January 1, 1997 (other than the taxable year of cessation or withdrawal), every registered limited liability partnership that has registered with the Secretary of State pursuant to Section 15049 of the Corporations Code and every foreign limited liability partnership that has registered with the Secretary of State pursuant to Section 15055 of the Corporations Code shall pay annually the tax prescribed in subdivision (a). The tax shall be paid for each taxable year, or part thereof, until any of the following occurs:

(1) A notice of cessation is filed with the Secretary of State pursuant to subdivision (b) of Sections 15050 and 15056 of the Corporations Code.

(2) A foreign limited liability partnership withdraws its registration

pursuant to subdivision (a) of Section 15056 of the Corporations Code.

(3) The registered limited liability partnership or foreign limited liability partnership has been dissolved and finally wound up.

(c) The tax assessed under this section shall be due and payable on the date the return is required to be filed under Section 18633.

AMENDMENT 6

On page 3, line 37, delete "SEC. 3." and insert:

SEC. 5

AMENDMENT 7

On page 4, delete lines 5 through 15, inclusive, and insert:

(b) A registered limited liability partnership or foreign limited liability partnership subject to tax pursuant to subdivision (b) of Section 17948 for which a notice of cessation has been filed pursuant to Sections 15050 or 15056 of the Corporations Code or for which registration has been withdrawn pursuant to Section 15056 of the Corporations Code, shall pay, for the taxable year of cessation or withdrawal, a tax equal to the amount specified in paragraph (4) of subdivision (d) of Section 23153 applicable for the taxable year of dissolution or withdrawal of a corporation. This subdivision shall not apply to a limited liability partnership doing business in this state after the effective date of the withdrawal of registration as provided in Section 15056 of the Corporations Code.

AMENDMENT 8

On page 4, delete lines 16 through 40, inclusive.

AMENDMENT 9

On page 4, after line 40, insert:

SEC. 6. Section 23153 of the Revenue and Taxation Code is amended to read:

23153. (a) Every corporation described in subdivision (b) shall be subject to the minimum franchise tax specified in subdivision (d) from the earlier of the date of incorporation, qualification, or commencing to do business within this state, until the effective date of dissolution or withdrawal as provided in Section 23331 or, if later, the date the corporation ceases to do business within the limits of this state.

(b) Unless expressly exempted by this part or the California Constitution, subdivision (a) shall apply to each of the following:

(1) Every corporation that is incorporated under the laws of this state.

(2) Every corporation that is qualified to transact intrastate business in this state pursuant to Chapter 21 (commencing with Section 2100) of Division 1 of Title 1 of the Corporations Code.

(3) Every corporation that is doing business in this state.

(c) The following entities are not subject to the minimum franchise tax specified in this section:

(1) Credit unions.

(2) Nonprofit cooperative associations organized pursuant to Chapter 1 (commencing with Section 54001) of Division 20 of the Food and Agricultural Code that have been issued the certificate of the board of supervisors prepared pursuant to Section 54042 of the Food and Agricultural Code. The association shall be exempt from the minimum franchise tax for five consecutive income years, commencing with the first income year for which the certificate is issued pursuant to subdivision (b) of Section 54042 of the Food and Agricultural Code. This paragraph only applies to nonprofit cooperative associations organized on or after January 1, 1994.

(d)(1) Except as provided in ~~paragraph~~ paragraphs (2) and (4), corporations subject to the minimum franchise tax shall pay annually to the state a minimum franchise tax of eight hundred dollars (\$800).

(2) The minimum franchise tax shall be twenty-five dollars (\$25) for each of the following:

(A) A corporation formed under the laws of this state whose principal business when formed was gold mining, which is inactive and has not done business within the limits of the state since 1950.

(B) A corporation formed under the laws of this state whose principal business when formed was quicksilver mining, which is inactive and has not done business within the limits of the state since 1971, or has been inactive for a period of 24 consecutive months or more.

(3) For purposes of paragraph (2), a corporation shall not be considered to have done business if it engages in other than mining.

(4) The minimum franchise tax for the taxable year of dissolution or withdrawal of a corporation shall be the amount specified in paragraph (1) for the taxable year of dissolution or withdrawal multiplied by a fraction the numerator of which shall be the number of months of the taxable year of dissolution or withdrawal, up to and including the month of effective date of dissolution or withdrawal as provided in Section 23331, and the denominator of which shall be twelve. This paragraph shall not apply to a corporation doing business in this state after the effective date of withdrawal as provided in Section 23331.

(e) Notwithstanding subdivision (a), a domestic corporation, as defined in Section 167 of the Corporations Code, that files a certificate of dissolution in the office of the Secretary of State pursuant to subdivision (c) of Section 1905 of the Corporations Code and that does not thereafter do business shall not be subject to the minimum franchise tax for income years beginning on or after the date of that filing.

(f) The minimum franchise tax imposed by paragraph (1) of subdivision (d) shall not be increased by the Legislature by more than 10 percent during any calendar year.

AMENDMENT 10

On page 6, line 26, delete "SEC. 5." and insert: